

## Message Text

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ACTION SS-14

INFO OCT-01 ISO-00 EUR-08 EB-03 SP-02 TRSE-00 NSC-05  
NSCE-00 FRB-01 CIAE-00 ONY-00 SSO-00 /034 W  
----- 011203 /42  
O 151335Z DEC 76  
FM AMEMBASSY LONDON  
TO SECSTATE WASHDC IMMEDIATE 8754

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E.O. 11652: N/A  
TAGS: EFIN' UK  
SUBJECT: SITUATION REPORT, DECEMBER 15

REF: (A) STATE 267168; (B) LONDON 20156

1. THE DEPARTMENT OF TRADE ON TUESDAY RELEASED ITS  
TRADE STATISTICS FOR NOVEMBER SHOWING A VISIBLE TRADE  
DEFICIT OF 510 MILLION POUNDS, THE THIRD LARGEST  
MONTHLY DEFICIT ON RECORD. THE CURRENT ACCOUNT WAS  
ESTIMATED TO BE 310 MILLION POUNDS IN DEFICIT IN  
NOVEMBER WHICH COMPARES TO OCTOBER'S 154 MILLION POUND  
DEFICIT. ALTHOUGH THE PRESS RELEASE EMPHASIZED THE  
INFLUENCE OF SPECULATIVE INCREASES IN OIL IMPORTS,  
THERE WERE FEW SIGNS OF ANY FUNDAMENTAL IMPROVEMENT IN  
THE U.K.'S EXTERNAL TRADE (LONDON 20216).

2. THE GUARDIAN HAS A FRONT PAGE STORY FROM JOHN  
PALMER IN BRUSSELS THAT AGREEMENT TO STABILIZE THE OVER-  
SEAS STERLING BALANCES WAS IN SIGHT AFTER A MEETING OF  
THE BIS WHERE BANKERS MADE CONSIDERABLE PROGRESS IN  
DEVISING A SCHEME TO PREVENT ANY FUTURE RUNDOWN OF THE  
BALANCES FORCING THE EXCHANGE RATE EVEN LOWER. WEEKEND  
DISCUSSIONS IN WASHINGTON WITH THE U.S. TREASURY AND  
FEDERAL RESERVE BOARD REPORTEDLY REVEAL A DESIRE ON THE  
PART OF THOSE CONCERNED TO ACHIEVE AN AGREEMENT OVER THE  
STERLING BALANCES.

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3. AN INCREASED TRADE DEFICIT AND STAGNANT INDUSTRIAL PRODUCTION FORMED THE BACKGROUND FOR A HARSH WARNING FROM THE PRIME MINISTER OF "UNPLEASANT SHOCKS" TO COME. CALLAGHAN TOLD THE COMMONS OF THE UNAVOIDABILITY OF A "PARTICULARLY DIFFICULT PERIOD" IN THE WAKE OF TODAY'S ECONOMIC PACKAGE. HE REPEATED HIS FIRM INTENT TO PRESS AHEAD DESPITE THESE DIFFICULTIES.

4. INDUSTRIAL PRODUCTION WAS VIRTUALLY UNCHANGED IN OCTOBER. OUTPUT HAS YET TO REGAIN ITS 1976 PEAK REACHED IN MAY.

5. FOREIGN EXCHANGE AND FINANCIAL MARKETS: THE FOREIGN EXCHANGE MARKET REMAINS NERVOUS AND EXPECT-ANTLY HOPEFUL PENDING THIS AFTERNOON'S MINI-BUDGET. THERE IS STILL A GENERAL FEAR THAT NOT ENOUGH WILL BE DONE, SUMMED UP BY THE ADVICE OF ONE FINANCIAL/BUSINESS COUNSELOR TO HIS CLIENTS: "IF THE COMING PACKAGE LEADS TO A SUFFICIENT CUT IN PSBR (1.5 - 2 BILLION POUNDS) FOR 77/78, WITH IMF MONITORING AND STRICT GUIDELINES ON MONEY AND CREDIT GROWTH IN 77 (10 PERCENT?), THEN YOU COULD SEE SHORT-TERM RATES TENDING DOWNWARDS IN JANUARY--I.E., MLR, (14-3/4 PERCENT) BANKS' BASE RATES (CURRENTLY 14 PERCENT) AND OVERDRAFT CHARGES -- THOUGH ONLY A POINT OR SO. ON THE OTHER HAND: IF THE CABINET SETTLES FOR ANOTHER 'COSMETIC' PACKAGE, WHICH HAROLD LEVER, LABOUR'S NOTORIOUS WHEELER-DEALER HAS

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NSCE-00 FRB-01 CIAE-00 ONY-00 SSO-00 /034 W  
----- 011205 /41

O 151335Z DEC 76  
FM AMEMBASSY LONDON  
TO SECSTATE WASHDC IMMEDIATE 8755

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BEEN STRENUOUSLY TRYING TO ARRANGE IN WASHINGTON, THEN  
SELL STERLING, GILTS AND EQUITIES IMMEDIATELY, AND  
COVER ALL YOUR FOREIGN EXCHANGE COMMITMENTS AS FAR  
AHEAD AS POSSIBLE."

IN TUESDAY'S TRADING THE POUND SHOWED SOME VOLA-  
TILITY. BUYING PRESSURE WHICH HAD BEEN STRONG IN  
NEW YORK AFTER LONDON'S MONDAY CLOSING INCREASED IN THE  
FAR EAST WHERE THE POUND TRADED NEAR \$1.69-1/2.  
LONDON'S BEST RATE CAME EARLY TUESDAY AT \$1.6925 AT  
WHICH TIME PROFIT TAKING EASED THE RATE BACK TOWARD  
\$1.68-1/2 WHERE IT TRADED UNTIL MID-AFTERNOON. SECONDS  
AFTER TRADE FIGURES WERE RELEASED SHOWING A MUCH HIGHER  
THAN ANTICIPATED DEFICIT FOR NOVEMBER, STERLING FELL  
BY OVER 1/2 CENT, AND CLOSED AT \$1.6760, DOWN \$0.0055  
ON THE DAY. ITS TRADE-WEIGHTED DEPRECIATION INCREASED  
TO 44.6 FROM 44.4 PERCENT. THE POUND OPENED THIS  
MORNING AT \$1.6815.

LOSSES IN THE GILT AND EQUITY MARKETS WERE ALSO  
ATTRIBUTED TO THE TRADE FIGURES. THE FINANCIAL TIMES  
INDEX OF 30 INDUSTRIALS FELL 9.4 POINTS TO 324.3.  
GILT PRICES FELL BY 3/8 POINTS ACROSS ALL MATURITIES.

SHORT-TERM INTEREST RATES EASED PERCEPTIBLY, PRE-  
SUMABLY THE RESULT OF THE AUTHORITIES' LARGE ASSISTANCE  
TO THE MARKET DURING THE PAST WEEK. THE 6 AND 3-  
MONTH STERLING CD NOTES FELL 1/4 PERCENT TO 12-15/16  
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PERCENT, AND 13-7/8 PERCENT, RESPECTIVELY.

ARMSTRONG

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